COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

Investigation by the Department of	**)**	
Telecommunications and Energy on its own	**)**	**D.T.E. 02-40**
Motion into the Provision of Default Service	**)**	

INITIAL COMMENTS OF TXU ENERGY RETAIL COMPANY LP

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EXECUTIVE SUMMARY

Massachusetts is at a crossroads in the restructuring of its electricity markets. This process, which began in earnest in 1997 with the passage of the Electric Restructuring Act, has brought many benefits to the citizens of Massachusetts. These include savings on electric bills, a well-functioning wholesale market, construction of clean and efficient gas-fired generating plants, a renewable resource portfolio standard, and funding for energy efficiency programs. Restructuring has not brought the benefits of retail competition to residential and small business customers, however, nearly all of whom remain on standard offer or default service. With the expiration of standard offer service fast-approaching, the Department must faces a clear choice: whether to take the steps necessary to bring the benefits of competition to all customers, or accept that residential and small business customers will continuing taking retail service from the incumbent utility for the foreseeable future. The Department should be commended for engaging this choice actively.

In these comments, TXU Energy Retail Company LP ("TXU") encourages the Department to take the actions required to bring retail competition to all customers, and describes what we believe those actions should be. TXU favors retail competition for all customers because of the benefits competition brings:

- Competition introduces better retail prices;
- Competition brings better service; and
- Competition brings innovative new products and services.

The comments then discuss why the current market structure has not allowed competition to take hold, bringing these benefits to consumers. Because the prices for retail services are still embedded in distribution rates, either retailers cannot recover their costs to provide those services, or customers will pay twice for them. Either of those results is unsustainable.

The comments then describe the general principles that should guide the Department in re-shaping the market to correct this fundamental flaw. These principles include:

- The role of the distribution company should be to focus on the reliability and security of the distribution network;
- Retail services should be delivered by separate, unregulated companies that focus on providing superior customer service and product innovation, forming direct relationships with end-use customers;
- Utility monopoly functions should be structurally-separated from competitive services, allowing utility affiliates to compete in the retail market without the risk of cross-subsidization; and
- A non-utility "supplier of last resort" would provide service to those who are not taking service from a retail provider, for any reason.

While implementing fully these principles would require legislative action, TXU also recommends that the Department consider the following actions, which it has the authority to take immediately:

- Make a strong statement in favor of retail competition and a retail market embodying the principles set forth above;
- Conduct a retail cost unbundling to identify the retail costs contained in utility distribution rates and re-align those costs in a more appropriate "retail" category;
- Open non-MBIS retail services to competition immediately; and
- Consider proposals that would allow the Department to select non-utility "alternate default service providers" that would be allowed to provide all retail services, including billing and information services, to default service customers.

TXU believes these proposals will keep Massachusetts moving toward the development of a robust retail market for all customers, and we urge the Department to consider adopting them. TXU also encourages the Department to reject proposals that that would tend to raise prices without bringing the benefits of competition to retail customers.

INTRODUCTION

This proceeding is a critical one for the future of electric restructuring in the Commonwealth. As the Department notes in its June 21, 2002 Order Opening Investigation into the Provision of Default Service ("Order"), the seven-year standard offer transition period will end in less than three years. Under the current law, all standard offer customers will become default service customers. TXU could not agree more with the Department's view that "the manner in which default service is made available to consumers could significantly affect the development of the competitive market." (Order at 2).

The Department faces a stark choice. One alternative is to continue the status quo with the distribution companies as the sole provider of default service. This all but guarantees that there will never be retail choice for the vast majority of ratepayers. The other alternative is to begin to make the structural changes in the electric market that will allow retail competition to thrive. This will provide all customers with a viable competitive alternative to remaining indefinitely on default service. Some of these structural changes require legislative action. We hope that one outcome of this docket is the Department's public support for the key concepts that should be contained in any new legislation. However, there are several important steps which the Department can take now to begin the process. TXU is pleased to describe these in detail below and respectfully requests that the Department give these options careful consideration.

I. TXU AND ITS INTEREST IN THIS PROCEEDING

TXU is one of the largest energy services companies in the world. Based in Dallas, Texas, TXU is part of a family of companies that is a global leader in electric and natural gas services, merchant energy, energy marketing, energy delivery, telecommunications, and other energy services. TXU

delivers or sells electricity and natural gas to a total of 11 million customers, primarily in the United States, Europe, and Australia. TXU has 2.7 million retail electric customers in the United States, making it the country's largest retail provider of electricity to residential customers.

TXU has taken an active interest in the Massachusetts market the Department's approach to electric restructuring. During the past year, TXU representatives have met with a number of legislators, regulators, utilities, customers, and other suppliers in order to understand where the Massachusetts electricity market is and where it may be going. TXU's interest in Massachusetts and in this proceeding is no secret. We would like to do business here, serving a large number of residential and small business customers, which is TXU's specialty. To do that, however, TXU believes the Department (and, possibly, the Massachusetts Legislature) will need to make certain changes to the structure of the retail electricity market. We appreciate the opportunity to provide these comments, which lay out certain measures TXU believes the Department can take to bring the benefits of retail competition to the citizens of Massachusetts. These comments take into account the unique characteristics of the Massachusetts market. Electric restructuring is not a "one size fits all" proposition, and what has been done elsewhere may not be appropriate here.

II. THE CURRENT STATE OF RETAIL COMPETITION

This investigation raises two fundamental questions about the current state and direction of the electricity market in Massachusetts. The first is whether the creation of a competitive retail market for electricity continue to be one of the Department's primary goals (and, if so, why)? The second is, if the retail electricity market should be opened to competition, does the current market structure, for retail

service generally and default service specifically, allow such competition to take hold and, if not, what can be done about it now and in the future?

A. The Retail Electricity Market Should Be Open to Competition.

To the first question, the answer is yes, without reservation. The Legislature made that statement explicitly in the 1996 Restructuring Act, and the Department has been steadfast in its support for the proposition that competition is better than regulation for the non-wires portion of retail electric service. How is it better? Competition is better than regulation because it benefits customers in three ways that regulation, no matter how enlightened, cannot:

1. Competition introduces better retail prices.

In a regulated market, large groups of customers pay the same price, in the same manner, on the same schedule, regardless of their individual needs or desires. In Massachusetts, nearly all of the 2.2 million residential customers pay either the standard offer service price or the default service price, and the only variation allowed is the choice between a six-month fixed price and a month-to-month price for default service. In a competitive market, customers demand, and suppliers supply, a smorgasbord of pricing and payment plans.[1] Some customers want the lowest price, and they will choose a discount provider. Some customers want help in managing their electricity use, and will focus on the total bill rather than just the price. Others may want a new service that is currently unavailable, and are willing to

[1] Wireless telephone customers, for example, can choose from an extensive array of plans, including pre-paid service in several forms.

pay for it. There is no doubt that competition will find better prices for retail electricity customers, as it has in other markets.[2]

2. Competition brings better service.

The very nature of regulated, cost of service rates discourages better service. A customer's request for anything other than what a utility provides currently means, if accommodated, additional expense in some form for the utility and, thus, is likely to be rejected. The Legislature and the Department have attempted to address this issue through the use of performance-based rates, but these efforts are designed mainly to prevent the deterioration of existing utility service, rather than encouraging utilities to discover and accommodate their customers' desires. In a competitive market, customers reward good service (and punish bad service) far more quickly and efficiently than can any legislative or regulatory body.

3. Competition brings innovative new products and services.

This is the most distinctive feature of competitive markets and the one that, in the long run, brings the most benefits to customers. Suppliers of any product or service, whether it be automobiles, telephones, or televisions, respond with innovation when challenged by competition. Although retail electric service is often dismissed as a "commodity," there is every reason to believe that true retail competition will bring the same kind of innovation to electricity

[2] While "better" may not always mean "lower" prices for every customer, it has been TXU's experience that, other things being equal, allowing a product or service to be provided by a competitive market rather than a monopoly tends to result in lower prices for that product or service. TXU expects that that would be the case with respect to the non-commodity retail services that are for the most part being provided only by regulated utilities in Massachusetts.

markets that it has to other markets.[3] In TXU's experience, customers associate their electric service with the things powered by that service, whether it be air conditioning, personal electronics, space heating, or an arc furnace. The customer's view of electric service, thus, provides as many areas for innovation as there are uses of that service. Electricity suppliers in a competitive market must adopt this view as well, and offer products and services tailored to the ways their customers use electricity. A monopoly provider's interest in innovation usually ends at the customer's meter.

B. <u>The Current Market Structure Has Not Brought Competition</u>.

The answer to the second question is that, for the great majority of Massachusetts customers, and nearly all of the residential and small commercial customers, there is no retail competition. The evidence on this point is irrefutable. According to the Division of Energy Resources' latest customer migration statistics, only seven of every 1,000 residential customers in Massachusetts take service from a competitive supplier. Even including small commercial and industrial, only 1.1 percent of mass market customers take service from a competitive supplier.[4]

While below-market standard offer rates may have delayed competition, they offer only a partial explanation of the near total failure of a retail mass market to develop. The more telling figure is that 40 times as many residential customers take default service as take service from a competitive supplier. The disparity in the number of default service customers versus those taking service from

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[3] TXU has seen such innovation even in the very short period of time that the Texas retail market has been open to competition. For example, TXU's retail affiliate recently developed a product that automatically dials the distribution company and several other telephone numbers when the electric service at a location is interrupted. This product has proven to be especially valuable for small businesses that rely on refrigeration but are not staffed around-the-clock. This product also shows that retail innovation can improve the performance of even the regulated part of a business, as it shortens the distribution company's response time to an outage.

[4] Based on statistics for May 2002. *See* http://www.state.ma.us/doer/pub_info/0205.xls.

competitive suppliers has continued despite the Department's decisive action to create a default service procurement process that results in default service prices reflecting market conditions. This alone, however, has not created the conditions necessary for retail competition to flourish for mass market customers.

In conducting this investigation, the Department clearly recognizes that the time is growing short to create a market structure that will allow retail competition to flourish where it has not. This investigation focuses on default service, and rightly so, as the current path leads directly to most customers reverting to default service as of March 1, 2005. Restructuring default service so that it brings more of the benefits of competition to the mass market is certainly one way to address this outcome, and below (Section IV.C.), we propose one method of doing so through the designation of an alternate default service provider. In some ways, however, this approach only addresses part of the problem. The lack of retail competition in Massachusetts is not caused primarily by the structure of default service, but by the structure of the market itself in which retailers compete against default service. TXU, therefore, encourages the Department to address these underlying obstacles to competition in ways that can be applied not only to default service, but to the structure of the retail market generally. Only with such action by the Department will TXU and other interested market participants truly be able to enter the Massachusetts retail electric market.

III. OBSTACLES TO RETAIL COMPETITION

The current lack of retail choice should come as no surprise. Many commentators predicted correctly that the standard offer would prevent retail competition, particularly in the earlier years when it

was deliberately priced below market. However, although the standard offer price has risen substantially, as has the number of default service customers, there has been no concomitant increase in retail competition. Assuredly, the Department has acted responsibly in permitting standard offer and default service to reflect true market costs. Allowing the default service price to reflect the wholesale price of power is sound public policy and produces significant benefits for customers. It is a prerequisite for retail competition, but is far from sufficient to achieve that goal.

An indispensable part of any viable market is that efficient participants must have a reasonable opportunity to reflect costs in the price of their service. The current market structure makes it all but impossible for even the most efficient retail provider to do so. We start from the indisputable premise that retail suppliers incur additional costs in serving customers other than the wholesale cost of the product which they provide. These costs cover services such as billing, customer service, credit and collections, marketing, and product development.[5] The essence of retail service is customer contact and any retail service provider must incur the personnel and equipment costs necessary to deal with a wide array of retail costs. If retail suppliers are allowed to compete only against the wholesale cost of electricity, and not the various retail costs, the economics simply do not work. That is, essentially, the status quo. Retail suppliers can compete only against the generation portion of default service or standard offer. For the most part, the retail supplier is paying the same wholesale market price as the distribution company for default service, hence, there is little if any customer revenue available to the

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[5] Throughout these Comments, we will use the term "retail services" to refer generally to the services such as those listed above, including billing, customer service, credit and collections, and marketing and product development, and the term "retail costs" to refer to those costs, other than commodity generation costs, that are incurred in serving retail customers. At this time, TXU would not include metering or metering costs within these terms. Section 312 of the Act currently prevents metering from being provided by the competitive market, and

retail provider after paying the wholesale price of power to offset even the variable costs of providing retail service, much less any margin.

Of course, retail suppliers have been making this point repeatedly to the Department. However, the remedy most often considered is to add some amount onto the wholesale default service price to represent "retail costs," including not only procurement and other administrative costs, (which utilities do incur in providing default service) but also marketing costs (which utilities do not incur in providing default service). The Department appropriately rejected the concept of including a "marketing" adder in default service prices. *Pricing and Procurement of Default Service*, D.T.E. 99-60-A (May 12, 2000). The Department sees that increasing the default service rate by adding costs utilities do not, in fact, incur to provide the service, or otherwise adding administrative costs to the default service rate without simultaneously removing them from distribution rates, artificially increases default service customer rates in order to encourage retail competition.

This approach turns public policy on its head. The Department's purpose in promoting competition is to provide benefits to customers – not to find ways to increase prices so competitors can compete. The Department has stated repeatedly that its mandate is not to create competition at all costs, but rather to put in place a market structure that allows efficient competition to thrive. *See Gas Unbundling*, D.T.E. 98-32-B at 30 (1999) ("Our role [in promoting competition] is not to guarantee the success of entrants. Rather, our role is to put in place the structural conditions necessary for an efficient competitive process – one where marketplace decisions of both producers and consumers are made on the basis of incremental costs"); *MCI WorldCom, Inc.*, D.T.E. 97-116-C (1999) at 35 ("The

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TXU believes that, for now, there is no compelling reason not to continue to treat metering as a distribution function.

Department has consistently rejected attempts over the years to make some customers and competitors better off at the expense of others, all in the name of promoting competition.")[6]

That is all we are asking the Department to do in this docket. TXU's proposals do not ask the Department to make accommodations designed to enable one supplier or a group of suppliers to better compete at the expense of customers or other suppliers. Rather, TXU encourages the Department to implement structural reforms that would allow entrants to take risks and compete efficiently -- with the benefits of such competition flowing to customers. These reforms address the single most pernicious obstacle to competition: customers paying twice for retail services.

Under the current market structure, every customer must take retail services such as billing and customer service from the distribution company. The distribution company's cost of providing these services is embedded in the monopoly distribution rates. Hence every ratepayer must pay for all these services in their utility bill. What possible economic benefit could there be in paying for them again to a retail provider?

Similarly, retailers will enter the market only when they have a reasonable opportunity to recover their costs and earn a profit. In the current market structure, that can only happen when there is a temporary divergence between wholesale prices and default service prices such that competitive suppliers can recover all of their costs, (wholesale generation and retail service costs as well), at a price

[6] Similarly, the Supreme Judicial Court has described the Department's function as "the protection of public interests and not the promotion of private interests." *Massachusetts Institute of Technology v. Department of Public Utilities*, 425 Mass 856, 872 n.38 (1997), quoting *Lowell Gas Light Co. v. Department of Public Utilities*, 319 Mass. 46, 52 (1946).

lower than the default generation price. These conditions are transient only, and as soon as they pass, competitive suppliers exit the market.

As we have seen over the past four years, both customers and retail providers have been acting in a manner consistent with their rational economic self-interest, hence, no retail market has developed. The reality is that so long as all retail costs such as billing and customer service are bundled into distribution rates and made part of monopoly service, there will be no meaningful opportunity for retail competition. Unless the Department and the Legislature take the necessary steps to create a new market structure, the only choice for the great majority of customers in March 2005 will be to remain on default service indefinitely. We set forth below our suggestions for steps the Department can take to address the development of a true retail market in the near- and long-term.

IV. WHAT THE DEPARTMENT CAN DO NOW.

We believe the Department can do three things in this proceeding to set the course for retail electricity markets.

?? Describe in detail the Department's vision for the future of the mass retail market in Massachusetts;

?? Immediately conduct a proceeding that would (1) identify the utilities' costs for all of the components of retail service currently included in distribution rates; (2) allow competitive retailers to provide those retail services to the maximum extent allowed by law; and (3) where not allowed (as in the case of billing services), allow for retailers to procure those services from the utility at tariffed rates ; and

?? Designate an alternate default service provider pursuant to G.L. c. 164, § 1B(d) that would replace the utility as default service provider and would be allowed to provide all retail services to default service customers.

Each of these actions would move Massachusetts much closer to making retail competition a reality for all customers by laying the essential foundation for TXU and others to enter the retail electric market.

A. The Department Should Make a Strong Statement in Favor of Retail Competition and a Market Structure that Achieves Retail Competition.

As several parties stated at the public hearing and technical conference, the Department should use this proceeding to lay out its vision for the structure of the post-standard offer market. For retail providers like TXU, it is critical to understand the Department's intentions before making the enormous investments necessary to enter the Massachusetts market. We urge the Department to make a statement that strongly favors retail competition for all, not just large commercial and industrial customers.

1. The Department Should Explicitly Identify Retail Competition As Its Goal.

It will not be enough in this proceeding for the Department to generally support the idea of retail competition; it must adopt retail competition for all customers as the central focus of these efforts. This action is important for two reasons. First, if a functioning mass retail market is the Department's goal for the end of the standard offer period, potential market participants must be convinced now of the Department's commitment to achieve that goal. A healthy retail market for residential and small commercial customers will develop by March 2005 only if competitors make substantial investments in the very near future to create such a market. If the Department does not state clearly and unequivocally

that its goal is to create a robust retail market for all consumers that will be in place and functioning by March 2005, potential competitors like TXU will not make such an investment in Massachusetts.[7]

Second, as was shown at the public hearing and technical conference, not everyone believes that retail competition for all consumers is a goal the Department should pursue. Some suggested that a pass-through of the wholesale market price, which is roughly what the current default service provides, is the best that consumers can hope for, and that the Department can declare victory and move on. Others suggested tentative measures that might result in some incremental increase in the number of customers nominally served by "competitive" suppliers, but are more likely to result in utility-provided default service becoming the de facto service of first and last resort for Massachusetts consumers. The Department should reiterate its view that all consumers have a right to enjoy the benefits of retail competition, and reject proposals and suggested measurements of "success" that are fundamentally inconsistent with this goal.

2. The Department's Vision Statement Should Describe a Market Structure that Will Allow True Retail Competition to Flourish.

In its Order, the Department stated that it would discuss measures that may be beyond its statutory authority to implement. *Order* at 6. We agree that the Department should look beyond its statutory authority and describe a market structure that corrects the fundamental flaws described above. TXU has described such a structure in a proposal that has been made publicly available, and TXU

[7] As discussed further below, this is one of the dangers of some of the proposals presented at the public hearing and technical conference that prolong the uncertainty around Massachusetts' commitment to a retail market. Rather than moving the State closer to retail competition, such equivocal measures will cause potential competitors to look elsewhere for new customers to pursue.

urges the Department to express support for the fundamental concepts contained in that proposal.[8] Those key concepts are as follows:

?? The wires functions of the distribution company should be carried out by companies whose single purpose is to focus on the reliability and security of the distribution network that delivers power to homes and businesses;

?? All retail services should be delivered by separate, unregulated companies whose single purpose is to focus on providing superior customer service and product innovation. These companies would form direct relationships with end-use consumers, resulting in new, value-added products and services. Incumbent utilities would be encouraged to create affiliates of this type and enter the retail marketplace;

?? Utility monopoly functions should be structurally separated from competitive services in order to simplify adherence to code-of-conduct requirements and reduce concerns about cross-subsidization; and

?? A non-utility "supplier of last resort" would provide service to those who are not taking service from a retail provider, for any reason.

While some of these measures, for example, structural separation of all retail functions, including billing services, are beyond the Department's present authority, a statement in support of this structure as the proper one for achieving the benefits of competition for all retail customers would be of interest to legislators who may consider these issues in the near future, and to potential competitors who are assessing the long-term attractiveness of the Massachusetts market.

[8] A copy of the proposal is attached as Exhibit 1 to these Comments.

B. The Department Should Conduct A Proceeding To Unbundle Retail Costs From Existing Distribution Rates, Thereby Re-Aligning those Costs and Re-Orienting the Customer Relationship to Allow for True Retail Competition.

As demonstrated above, the essential part of a market structure that will allow retail competition to exist for more than the largest customers is the unbundling of competitive retail functions from the monopoly distribution function. This requires the identification of all costs not associated with providing the wires services and the separation of those costs from the distribution charge. While the Department describes this proceeding as an investigation into default service, any restructuring of default service that does not address the amount and appropriate rate treatment of retail costs, not only for default service but for all retail service, will not allow retail competition to succeed. Once these non-wires charges are identified and separated from the distribution rates, customers should have the right, to the maximum extent allowed by law, to purchase these services from a retailer and not be forced to purchase them from the distribution company if there are lower priced or better alternatives. This will give retail providers the opportunity to compete with the distribution companies to provide these services at a lower cost, providing real choice and economic benefits to all customers.

Where present law does not allow for retailers to provide these services themselves (as in the case of billing services), the Department should allow retailers to purchase these services from utilities, at least temporarily, at tariffed rates established during the rate unbundling proceeding. These measures, all of which are well within the Department's current authority, will re-orient the market structure (for both default service and competitive retail supply) from one in which the distribution company dominates to one in which the customer looks to the retailer as its electricity provider. Such a re-orientation would encourage competitive suppliers to enter the Massachusetts market on a permanent basis.

1. Partial Retail Services Unbundling.

As discussed above, the unbundling of retail services from distribution rates is the *sine qua non* of any market structure that will permit the opportunity for retail competition. Unless preceded by this key action, any substantive step the Department takes to prepare for the expiration of standard offer service, including any restructuring of default service, will be ineffectual in creating true retail competition. Implementing this process will require cost unbundling proceedings for each of the distribution companies. In light of the time for such an undertaking, we urge the Department to begin this process immediately while the Legislature considers changes to the Act. Such unbundling proceedings will allow the Department to take the other steps discussed below that will move Massachusetts toward a competitive retail market.

a. The Department has the authority to conduct a rate unbundling proceeding.

The Department's general supervisory powers allow it to require distribution companies to conduct unbundling studies and file them with the Department. G.L. c. 164, § 76 provides the Department with general authority over electric companies:

> The department shall have the general supervision of all gas and electric companies and shall make all necessary examination and inquiries and keep itself informed as to the condition of the respective properties owned by such corporations and the manner in which they are conducted with reference to the safety and convenience of the public, and as to their compliance with the provisions of law and the orders, directions and requirements of the department; . . . .

G.L. c. 164, § 76.[9]

[9] In DTE 99-60-A, the Department expressed it intention to "use the full measure" of its § 76 authority in its supervision of default service procurement practices to ensure that those practices are reasonable. *Default Service Investigation*, DTE 99-60-A, at 16 n.15 and 17.

In *Boston Edison Co. v. Department of Public Utilities*, 375 Mass. 1, 44, *cert. den.* 439 U.S. 921 (1978), the Supreme Judicial Court described the Department's authority as follows:

> Under G.L. c. 164, the Department possesses broad investigative and supervisory authority over electric utilities and may properly inquire into these aspects of their operations in furtherance of its mandate to `keep itself informed as to . . . the manner in which they are conducting with reference to the . . . convenience of the public.' G.L. c. 164 § 76.

Other provisions of Chapter 164 also authorize the Department to conduct inquiries and gather information. General Laws c. 164, § 83 provides that utilities and their managers "shall at all times, upon request, furnish any information required by the department or its duly authorized employees relative to their condition, management and operation, and shall comply with all lawful orders of the department . . . ." Similarly, Section 85 provides that "[t]he officers and employees of the department may be authorized by it to examine the books, contracts, records, documents and memoranda or the physical property of any company subject to this chapter . . ."

In *Boston Real Estate Board v. Department of Public Utilities*, 334 Mass. 477 (1956), the Supreme Judicial Court discussed in detail the Department's authority under G.L. c. 164, § 94. The case arose when Boston Edison filed a tariff that, for the most part, eliminated the competitive resale of electricity purchased from Boston Edison. The Department, reviewing the tariff pursuant to its authority in § 94, approved that aspect of the tariff, finding the practice of competitive resale to be "fundamentally unsound and against the public interest." On appeal, the plaintiffs argued that § 94 gave the Department jurisdiction only over utility "rates, prices and charges" and changes thereto, but not over a utility practice such as competitive resale. The Court rejected this narrow interpretation of the Department's authority under § 94, finding that "[r]ate practices as well as rate scales may be regulated under a power to prescribe rates." The Court found further that the amendment of § 94 in 1927, St.1927, c. 316, § 2,

significantly broadened the power of the Department, and that those powers now included not only authority over "the stated rates, prices and charges for various classifications of service, and the relationship between classifications, but also over reasonably related terms and conditions stated in the service contract or the filed schedules" and, indeed, "jurisdiction of the entire rate structure." *Boston Real Estate Board v. Department of Public Utilities*, 334 Mass. at 484-85.

The broad supervisory power granted to the Department by the Legislature provides ample authority for the Department to conduct an investigation into the appropriate classification of rates for various retail services that are currently included in distribution rates. The Department would also have the authority to change the classification of the rates for those retail services, moving them from distribution to a more appropriate category associated with competitive electricity supply. The Department considered performing such a realignment of administrative costs in D.T.E. 99-60-A, and did not do so for reasons other than a lack of authority to move those price elements out of distribution rates. D.T.E. 99-60-A at 19. The Department's Order also stated the Department's intention to consider "the price components to be included in default service rates, including administrative and bad debt costs and the effects of locational marginal pricing." *Order* at 6. The Department clearly has the authority to consider *all* prices components that should be removed from distribution rates and included with generation to create a "retail" service price against which retailers could compete fairly.

b. The Department has the authority to open non-MBIS retail services to competition.

The Department can do more than identify the retail components of distribution rates and move those components to a proper retail rate category. We also submit that, in the absence of a legislative

prohibition to the contrary, the Department has the authority to unbundle non-monopoly retail services from the distribution rates and make them subject to competition.[10]

The Department's broad supervisory authority over electric utilities, as described above, gives the Department discretion to allow retail suppliers to provide retail services, in addition to commodity generation, in competition with incumbent utilities. In addition, the Department was given an explicit directive by the Legislature to "require electric companies organized pursuant to the provisions of this chapter to accommodate retail access to generation services and choice of suppliers by retail customers, unless otherwise provided by this chapter." G.L. c. 164, § 1A(a). This directive provides the Department with further authority to properly align services to allow for true retail access.

Moreover, throughout the restructuring process, the Department has recognized that it has extensive authority to unbundle services and subject them to competition (where that authority is not otherwise explicitly held in check by the Legislature). With its order in *Electric Industry Restructuring*, D.P.U. 95-30 (August 15, 1995), the Department moved decisively toward creating competition for generation services, more than two years before the Legislature passed the Act, which gave the Department specific direction as to how that restructuring should proceed. In *Electric Industry Restructuring*, D.P.U. 96-100 (December 30, 1996), the Department found that it had the authority not only to order the unbundling of generation from distribution and transmission, but also to order the further unbundling of retail services that would remain with the distribution company:

> The authority to prescribe which services may be subject to competition is closely related, and flows naturally from actions already within the purview of the Department. Although the power to create or amend franchise service territories may be reserved to the

[10] As discussed above at n. 4, TXU believes that metering services, including meter reading, should remain part of distribution service unless and until the Legislature finds that metering should be opened to competition.

> Legislature, we conclude that the Department has the authority to determine which distribution functions should be provided competitively in the future.

D.P.U. 96-100 at 101. *See also* D.P.U. 95-30 at 39-43 (discussing Department's authority to unbundle rates for generation, distribution, and transmission).

The breadth of the authority the Legislature gave to the Department is shown by the instances in which the Legislature chose to restrain that authority. The most notable is the Legislature's treatment of metering, billing, and information services ("MBIS"). MBIS is truly the exception that proves the rule. Section 312 of the Act directs the Department to undertake an investigation of the costs and benefits to Massachusetts customers of unbundling and creating retail competition for MBIS. Section 312 states further that, should the Department determine that MBIS should be subject to unbundling and competition, "said department shall, by no later than January 1, 2001, file its recommendations, along with drafts of legislation necessary to implement said recommendations, with the clerk of the house of representatives."

The Legislature went on to say, however, that "[a]ny unbundling and creation of retail competition of such [MBIS] services shall not commence unless statutorily allowed through amendments to said chapter 164 upon said department's compliance with the provisions herein." If the Department did not otherwise have the authority to unbundle and create retail competition for MBIS, the Act's prohibition against such action without further legislative action would have been unnecessary, rendering the sixth sentence in Section 312 "mere surplusage." The Department has consistently found that such interpretations of its enabling legislation violate accepted canons of statutory interpretation.[11]

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[11] *See, e.g., Default Service Investigation*, D.T.E. 99-60-A (May 12, 2000). *See also Town of Milford v. Boyd*, 434 Mass. 754, 757 (2001); *Boston Police Patrolmen's Ass'n, Inc. v. City of Boston*, 435 Mass. 718, 721 (2002) (statutes should be interpreted so as to avoid rendering any part of the legislation meaningless).

c. Opening Non-MBIS Retail Services to Competition Would Benefit Consumers Now.

While the Department cannot open "MBIS" to competition, there are other retail services that it can allow retailers to provide. In TXU's experience, these non-MBIS services can be critical to developing customer relationships, and allowing retailers to provide these services, and removing any costs associated with these services from distribution rates, would benefit customers immediately. These non-MBIS retail services include:

- Customer service, including customer inquiry and account management services;
- Credit and collections;
- Sales and marketing;
- Product development;
- Wholesale procurement (to the extent not included in wholesale generation costs); and
- Advertising.

Neither Section 312 of the Act nor any other statutory provision prohibits the Department from opening these retail services to competition and, based on the results of a cost unbundling proceeding, removing the costs of those services from distribution rates. For example, in its Report to the Legislature pursuant to Section 312, dated December 29, 2000, the Department defined the following as the billing and information services that should not be opened to competition: (1) the calculation of bills based on metered consumption data and the applicable prices; (2) the preparation and distribution of the invoice; (3) the transmission of the billing data to competitive generation suppliers; and (4) the receipt of account payables and disbursement of payments to the distribution company and the

generation service provider. No member of the legislature nor any interested party has taken issue with this definition.[12]

We acknowledge that the Department cannot create competition for these billing and information services absent legislative authorization. As shown above, however, the Department has ample authority to unbundle and create competition for the other retail services listed above.[13] Unbundling these other retail services would be a significant step toward the creation of a retail market. It would not only allow retail providers the opportunity to compete with distribution companies to recover these costs from customers, but would also provide the opportunity for the kind of direct customer interface that is so vital to the retail business. While TXU will continue to advocate that the Legislature allow competition for billing, we urge the Department to immediately begin the unbundling process and make significant progress toward making retail options available to all consumers.

d. A rate unbundling proceeding would identify the non-MBIS services that should be opened to competition, allow the Department to take steps to mitigate any negative impacts on utilities, and provide retailers with an efficient route of entry into the market for these services.

A rate unbundling proceeding would do more than separate utility distribution rates into "wires" charges and various retail components. It would also accomplish three practical and important goals. First, it would identify all of the non-wires services that should be removed from distribution rates and

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[12] While at least one utility sought to include substantially all of its customer service functions in the definition of MBIS, the Department did not adopt this broader view in its report to the Legislature. *C.f. Joint Comments of the NSTAR Companies* at 6-7, and *Report to the General Court on Metering, Billing and Information Services* at 4-5.

[13] The list above is based on the Massachusetts utilities' filings in D.T.E. 00-41 and on TXU's experience in providing retail service to 11 million customers in North American, Great Britain, and Australia. A complete list of retail services being provided by utilities in Massachusetts can be generated only by examining the utilities' rates in the context of an unbundling proceeding.

placed in a new "retail services" rate category. While some of these services are apparent from filings made during the Department's MBIS investigation, only a detailed review of utility cost data will reveal all of the services that are rightly considered "retail" rather than "wires" services. Second, within the retail service category, the Department can further differentiate between MBIS services, which cannot be opened to competition, and other retail services which, as discussed above, can and should be opened to competition.

Finally, the findings in the rate unbundling proceeding would enable utilities to file cost-based tariffs for all retail services. Such tariffs would serve several important functions. They would allow retailers who wished to enter the Massachusetts market to procure some or all of those services on a wholesale basis from the incumbent utility (so long a the Legislature allows the utilities to remain in the retail business). This would mitigate any negative impacts on utilities from opening non-MBIS retail services to competition by creating a market for those services among competitive suppliers. At the same time, the availability of utility services on a tariffed basis would provide retailers with an efficient route of entry into the Massachusetts market. Where a particular retailer could provide a service more cheaply than the utility, it would do so; where the retailer could procure those services more cheaply or at higher quality from the utility, it would do so. As discussed below, these tariffs would also play an important role in the re-orientation of the customer relationship through the alternative delivery of billing services or the designation of an alternate default service provider.

2. Section 312 Notwithstanding, the Department May Still Create a Structure for the Delivery of Billing Services that is More Consistent with Retail Competition.

While Section 312 prohibits the Department from opening billing services to competition, the Department can still create a structure for billing services that is more consistent with retail competition. Much has been written about the potential costs and benefits of a "supplier single bill," in which the supplier bills and collects for all electric charges, not just the charge for generation. In its MBIS report, the Department found that the supplier single bill "can be readily accommodated within the existing regulatory framework by requiring distribution companies to offer a third billing option to customers and competitive suppliers." MBIS Report at 28. Unfortunately, when the Department examined this issue further, it concluded that none of the options presented to it for the supplier single bill could be accommodated without violating either G.L. c. 164, §1D, regarding the billing options to be made available to customers, or Section 312's prohibition against opening billing services to competition.

By requiring utilities to file tariffs for all retail services, including billing services, the Department can create a structure for the delivery of billing services that will gain most of the benefits of a supplier single bill while both complying fully with the Act and avoiding some of the drawbacks of a supplier single bill identified in D.T.E. 00-41. This would be accomplished by requiring retailers to buy (and utilities to sell) utility billing services at cost-based tariffed rates. In this manner, utilities would continue to "create and send bills to retail customers" as required by G.L. c. 164, § 1D. The difference would be that, with the exception of the presentation of distribution and other regulated rate information and detail, the retailer would control the content and format of the bill, and could change it to fit the retailer's business goals. Discount retailers could simply take the utility bill as currently presented, with no

additional information or identification. Retailers wishing to establish a premium brand identification could buy enhanced services from the utility (which would be acting as the retailer's billing services vendor), adding logos or new product and service promotions as the retailer saw fit. The bill would become a vehicle for the retailer to establish a true retail relationship with the customer, even as the utility remained the monopoly provider of billing services.[14]

Such a system would implicate none of the concerns raised about competitive billing in D.T.E. 00-41 and D.T.E. 01-28, Phase II. The utility would continue to "create and send bills to retail customers" in what would amount to a variation of the "utility single bill" described in G.L. c. 164, § 1D. Bills would continue to be as accurate and timely as they are now. Utilities would continue to be the collections agent for all funds. No utility personnel would be displaced, as there would be no decrease in the demand for billing services. In fact, it is likely that there would be increased demand for such services as retailers sought enhanced billing services to create brand awareness and promote new products and services.

In short, there would be no downside to creating such a structure for the delivery of billing services. While TXU would prefer to see the Legislature open billing services to competition, this proposal would be an important interim step that the Department can implement now with its present statutory authority. This measure, along with the unbundling of non-MBIS retail services, would re-align prices and re-orient the customer relationship to create a market structure that would support a fully competitive retail market.

[14] In any event, the utility would also remain the monopoly provider of collections services, remitting funds to the retailer pursuant to the Department's *pro rata* directive in D.T.E. 01-28, Phase II.

C. Alternate Default Service Option.

By implementing the steps described above, the Department could transform default service into a true retail service, allowing retailers to compete on an equal footing in offering alternatives to default service. These steps alone, however, may not ensure the creation of a robust retail market by the time standard offer service expires in early 2005. Retailers like TXU will be much more interested in entering the Massachusetts consumer market in the next two years if they can do so with scale, rather than one customer at a time. Scale entry allows a retailer to generate sufficient revenue to begin covering the significant capital expenditures required to do business in a complex industry such as retail electricity. Utilities already enjoy this scale due to their position as incumbent providers to the mass market.

The Department can use default service to provide retailers like TXU with an opportunity for such scale entry by designating non-utility retailers to act as "alternate default service providers" pursuant to G.L. c. 164, sec. 1B(d).[15] The Department could do so through one of two routes. It could conduct an auction of utility default service customers, as described in the joint retailer comments, or it could entertain a petition from one or more retailers to displace the utility as default service provider. The Department has ample authority to take either of these actions. The Department also has the authority to allow an alternate default service provider to supply all retail services, including billing and information services.

[15] While TXU favors the selection of "alternate default service providers," as allowed by G.L. c. 164, §1B(d), TXU does not recommend that standard offer service customers be moved from that service before the expiration of the transition period in February 2005.

1. The Department has the authority to designate a non-utility default service provider.

The plain language of G.L. c. 164, § 1B(d) gives the Department the authority to authorize an alternate generation company or supplier to provide default service: "The department may authorize an alternate generation company or supplier to provide default service, as described herein, if such alternate service is in the public interest." G.L. c. 164, § 1B(d). Where the language of a statute is clear, the Department must give effect to its plain and ordinary meaning.[16] The language of § 1B(d) is perfectly clear: a company other than the utility can provide default service.[17]

2. An Alternate Default Service Provider May Provide the Same Retail Services that the Utility Provides When Acting as the Default Service Provider.

Selecting non-utility retailers to act as alternate default service providers will not help the retail market develop in Massachusetts if they are only allowed to provide generation service. That is, in essence, the system that is in place now. The utility provides all retail services and non-utility wholesalers supply the electrons. A plan that keeps this system in place and nominally re-casts the wholesale suppliers as "retailers" will do nothing to bring the benefits of competition to Massachusetts consumers. Fortunately, the statute allows an alternate default service provider to provide any or all of the services provided by the utility, including retail services such as billing and information services.

This is clear from the Act's definition of "default service." "Default service" is defined as "electricity services provided to" certain retail customers (including, "all customers" not receiving generation from a competitive supplier after the standard offer term expires). G.L. c. 164, § 1

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[16] *Town of Milford*, 434 Mass. 754, 756, quoting *Massachusetts Broken Stone Co. v. Weston*, 430 Mass. 637, 640 (2000).

(definitions). "Electric service" is defined as the "provision of generation, transmission, distribution or ancillary services." G.L. c. 164, § 1 (definitions). Thus, a company that provides "default service" may provide any or all of "generation, transmission, distribution, or ancillary services."[18]

The context of § 1B(d) also supports the interpretation that an alternate default service provider can provide retail services other than generation. The statute requires that the utility procure default service through competitive bidding, and that "[a]ny department-approved provider of service, including an affiliate of a distribution company, shall be eligible to participate in the competitive bidding process." Thus, when default service is provided by a distribution company, the utility provides all of the retail services, and a non-utility entity provides the commodity generation service. If the "alternate generation provider" could provide nothing other than commodity generation service, the arrangement would be no different than when the distribution company provides default service. This interpretation would render the "alternate generation provider" language in § 1B(d) superfluous. *See, supra*, n.9. [19]

Moreover, the provisions of the Act that have otherwise limited the Department's authority to act in the area of certain retail services, like billing, do not preclude the Department from authorizing an

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[17] At the July 23 public hearing and technical conference, one utility also suggested a plan in which the Department would use its authority under § 1B(d) to designate non-utility default service providers.

[18] A reading of the statute that allows the various definitions to accommodate a market structure in which retailers provide more than generation is also sensible given the options for further market development contemplated by the Act. As discussed in Section IV.B.1.b., above, the Department has the authority to unbundle other retail services and open them to competition, and was prevented from doing so in the case of billing and information services only by Section 312 of the Act. Section 312 itself, however, recognizes that the prohibition against unbundling MBIS may only have been temporary; had the Department recommended this action to the Legislature, some or all of those services might be open to competition now. It seems unlikely that the Legislature would have drafted the basic definitions in the Act to accommodate only the possibly temporary suspension of the Department's broad authority to open services to competition.

[19] The Department's regulations implementing the Act also support the interpretation that default service can include service components other than commodity generation. In 220 CMR 11.02, the Department does not define "Default Service," but rather "Default Generation Service." If the term "Default Service could only mean generation service, the Department's use of the term "Default Generation Service" would be rendered a redundancy." The

alternate generation company or supplier from providing retail-related services. As discussed above, Section 312 of the Restructuring Act restricted the Department's authority to order the "unbundling and creation of retail competition" for MBIS. When provided by an alternate default service provider, however, billing and information services would be neither unbundled nor opened to retail competition. They would remain part of a bundled default service that could be offered only by a Department-designated alternate default service provider, not by competitors at large.

Further, Section 1D's requirement that distribution companies "create and send" bills in either the utility single bill or dual bill formats does not preclude this result. Section 1B(d) states that an alternate generation company or supplier can "provide default service, **as described herein**" (emphasis added). As discussed above, the default service "described herein" is best understood as a bundled service, including billing and information services, and a reading of §1D that would conflict with this interpretation sets up an unnecessary conflict between §1B(d) and §1D. This conflict can be avoided by interpreting §1D as the plain language indicates: the two-bill option applies only when it is the distribution company that "creates and sends bills to retail customers," not in the narrow circumstances in which the Department designates an alternate generation company or supplier to provide those services pursuant to §1B(d). It is a basic canon of statutory interpretation that "general statutory language must yield to that which is more specific."[20]

Department, cognizant of the Act's broader definition of "default service" that includes "electrical services" generally, chose to define only one component of default service, namely "default generation service."

[20] *TBI, Inc. v. Board of Health of North Andover*, 431 Mass. 9, 18 (2000), quoting *Risk Mgt. Foundation of Harvard Med. Inst. v. Commissioner of Insurance*, 407 Mass. 498, 505 (1990).

3. The Statute Allows the Department to Accommodate Several Varieties of Alternate Default Service Providers.

General Laws c. 164, § 1B(d) does not prescribe a single means by which alternate default service must be provided. Further, the statute **allows**, but does not **require**, alternate default service providers to provide the full range of retail services along with generation, as utilities do now. This statutory scheme gives the Department the flexibility to accommodate several versions of alternate default service. For example, the Department could entertain petitions from prospective alternate default service providers, which could range from full-service retailers like TXU, who would be interested in providing directly all retail services, to more specialized companies interested in providing some subset of those services. The filing of utility tariffs for these various services, as described in Section IV.B. above, would facilitate such a range of alternative proposals.[21]

Whatever the arrangement, however, any alternate default service proposal must be shown to be "in the public interest."[22] The public interest requirement will constrain both suppliers and utilities from proposing alternate default service arrangements that do not provide the benefits of competition to Massachusetts consumers, or that try to provide those benefits by raising prices beyond what customers would otherwise pay. For that reason, TXU recommends that the Department only consider "alternate default service provider" arrangements after it has examined and unbundled the utilities' costs to provide

[21] The Department could also conduct a retail auction that would allow retail "alternate default service providers" to completely replace distribution companies as default service providers. This option is discussed in greater detail in the Initial Comments of the Competitive Retail Suppliers. TXU supports the concept of such an auction, but only if it is accompanied by the rate unbundling and structural reforms recommended above.

[22] While the Department has not yet had the opportunity to apply the public interest standard in the alternate default service context, TXU suggests that the Department consider, at a minimum, such a proposals impact on prices, quality of service, and competition. *See, e.g., NIPSCO-Bay State Acquisition*, D.T.E. 98-31 (1998), at 10; *Eastern-Essex Acquisition*, D.T.E. 98-128 (1999), at 8-9.

retail services, as described in Section IV.B.1. In that way, the Department can ensure that the costs of any retail services provided by the alternate default service provider are removed from distribution rates so that customers do not pay twice for those services.

D. The Department Should Reject Proposals that Will Raise Retail Prices and Bring No Benefits of Competition to Consumers.

Admittedly, TXU's proposals are designed toward introducing a viable retail option to all customers by 2004 in preparation for the end of the standard offer transition period in early 2005. That leaves open the question of what the Department should do regarding default service in the short-run before cost unbundling is complete. Quite simply, we suggest that the Department make no change to default service. Default service, as currently arranged, does an excellent job of providing customers the benefits of a competitive wholesale market. As most commentators at the public hearing agreed, restructuring has led to a highly competitive wholesale market with several vigorous competitors who have provided default generation service to the distribution companies.

At the public hearing and technical conference, the Department heard several proposals that purported to change default service with the goal of introducing retail competition into the mass markets in time for the expiration of standard offer service. As described to date, these proposals would not accomplish this goal. Rather, they would only raise prices and actually serve to discourage potential retail providers from entering the Massachusetts market. Such proposals should be entirely rejected.

One such proposal has as its key feature that the utility would "exit the retail market" by transferring to retail suppliers the utility's responsibility for procuring generation for default service. The

flaw in this proposal is that the risk associated with procuring generation is the only thing that would be given to the putative "retail" supplier. All retail services, including billing, customer service, and collections, would continue to be provided by the utility acting as a monopoly. This is simply wholesale supply dressed to look like retail service.

Only the utility would benefit in this scheme. Customers will see higher prices and both wholesale and retail suppliers will be discouraged from participating in the market. The wholesale suppliers who currently provide generation default service will be required to become licensed competitive suppliers and incur significant additional costs. For example, a wholesale supplier currently providing default service generation to the utility has little concern regarding bad debt (since it has only one contract, and that is with the utility). Under the proposed new scheme, the supplier taking on default service load would have to account for the bad debt associated with having contracts directly with retail customers rather than one contract with the utility. In this arrangement, the utility would have passed its bad debt costs on to the "retail" default service providers but, as we know from D.T.E. 99-60-A, those costs are currently embedded in distribution rates. Thus, default service customers would pay twice for the costs of bad debt associated with the service.

The scheme would also require the default service provider to pay for the costs of EDI in switching customers and exchanging other information with the utility. In the current default service system, in which the utility is default service supplier of record, any such costs incurred by the utility are, again, embedded in distribution rates. Default service providers would also have to provide additional customer service functions, that, again, are duplicative of those included in distribution rates. All these additional costs will inevitably be reflected in higher default service prices.

Other than potential benefits to utility shareholders from mitigating future risks associated with wholesale procurement, plans of this type are lose/lose propositions to both consumers and competitors. As demonstrated above, consumers will be paying higher prices for default service and receiving no additional benefits other than duplicative retail services they are already paying for in distribution rates.

Wholesale suppliers, who are active participants in the default generation market, may decide to withdraw from the Massachusetts market rather than assume the risks and responsibilities of a retail provider. Retail providers, like TXU, will not find this market structure attractive because it will not be sustainable over the long run. It will result in higher prices for customers and no meaningful customer contact for the retail providers. A viable retail market cannot be built on such a shaky foundation.

CONCLUSION

TXU is greatly encouraged by the leadership the Department has shown in taking on the challenging issues set forth in the Order. Having gone through an extensive restructuring process in Texas, making the transition from an integrated utility to a structurally-separated retail supplier, TXU can attest that there are no easy answers to the questions the Department has posed, and we suggest none. In fact, the rate unbundling TXU recommends is a time-consuming and difficult undertaking. But TXU believes strongly that the Department will agree that this is the only way to bring the benefits of true competition to the Massachusetts retail market, and that there is no time to lose in starting to work toward that goal. Without a true retail service for retailers to compete against, true competition and the benefits it can bring to consumers will not be realized.

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